

---

**(1995) 12 KAR CK 0047**  
**In the Karnataka High Court**  
**Case No : T.A. and E.T. 3 and 4 of 1993**

Arya Bhavan

APPELLANT

Vs

State of Karnataka

RESPONDENT

---

**Date of Decision :** 20-12-1995

**Acts Referred:**

Factories Act, 1948 — Section 15

**Citation :** (1996) ILR (Kar) 1262

**Hon'ble Judges :** M.F. Saldanha, J; Chandrashekaraiyah, J

**Bench :** Division Bench

---

## Judgement

M.F. Saldanha, J.—A rather ticklish question of law has been raised by the appellants in these two appeals which requires in our considered view, a decision within the scope and context of the Karnataka Tax on Entry of Goods into Local Areas for Consumption, Use or Sale Therein Act as contra-distinguished from the view taken by the courts from time to time in relation to several other enactments. The controversy centres around the question as to whether the appellants, who basically run restaurants in the city of Bangalore, but who are famous for some of their specialised preparations mainly sweets and other edible items, can be regarded as a manufacturing unit within the meaning of entry No. 16-B of the Act. For the purpose of convenience, we have extracted entry No. 16-B along with the explanations which read as follows :

"16-B. All raw materials, component parts and inputs which are used in the manufacture of an intermediate or finished product, or in the processing, improvement or repairs of goods, -

(i) when brought into local areas by an industrial unit, or

(ii) when brought into local area by any dealer who, after having so brought, sells or supplies the same to an industrial unit located either within the same local area or outside it.

Explanation I. - The words "industrial unit" mean, a manufacturing unit which

falls within the definition of a "factory" under the Factories Act, 1948 (Central Act No. LXIII of 1948), but excludes, - (i) handicrafts manufacturing units,

(ii) handloom weaving units, and

(iii) any other group or class of industries which may with reference to their nature, competitiveness, employment potential or such other factors, be notified by the State Government.

Explanation II. - The words "raw materials, component parts and inputs" do not include agricultural produce, horticultural produce, timber or wood of any species, silk cocoons, raw, thrown or twisted silk, tobacco (whether raw or cured), cement, paper, electrical goods,

.....

or, such other inputs as may be notified by the State Government for purposes of exemption from tax under item 16-B from time to time, but include aluminium ingots and ores of all kinds."

We need to clarify, that Explanation I has subsequently been amended by virtue of Karnataka Act No. 18 of 1989 and the amendment is also set out below :

"(2) in explanation I to item 16-B for the words, figures and brackets "which falls within the definition of a factory under the Factories Act, 1948 (Central Act No. LXIII of 1948)" the words, figures and brackets "whose total turnover in a year under the Karnataka Sales Tax Act, 1957 is not less than rupees ten lakhs" shall be substituted."

2. By virtue of these provisions, what is sought to be taxed is the inputs used in the manufacturing of an intermediate or finished product when brought into the local areas by an industrial unit which in turn by virtue of the explanation is construed to mean a manufacturing unit. The appellants' basic contention is that the activity carried on by them regardless of the scale on which it is carried out effectively consists of a process of producing various edible items and that consequently, it cannot be treated on par with a manufacturing unit. The submission is that viewed from any angle, the activity is no different virtually from one of cooking in so far as it is an amalgamation of the various ingredients and merely because it is done on a bigger scale and provided to customers, that it would not change the complexion of the process. The appellants therefore contend that under no circumstances can entry No. 16-B be made applicable to their business and that they are therefore entitled to be totally excluded from the operation of the Act. As indicated by us earlier, the next point of law that arises is as to whether within the provisions of law that we have extracted above, the appellants can be construed to be a manufacturing unit or an industrial unit within the connotation of the provisions.

3. The appellants' learned advocate quite apart from pointing out to the court in his submission that the activity carried on by his clients is no different to the

normal processes that are carried out in every home, except that these are done on a larger and commercial basis and are provided to customers has made a strong appeal to the court that these aspects of the matter be duly taken cognizance of and that the department's equation of their business with a manufacturing unit or an industrial unit should be disallowed. The controversy had arisen because the assessing officer took the view, as far as the appellants are concerned that they do not qualify for payment of tax whereas the Commissioner of Commercial Taxes exercising his revisional powers u/s 15 of the Act, after hearing the appellants passed orders in respect of two assessment years, holding that the exemption was wrongly granted and that the appellants are liable to be assessed. It is against these orders that the present appeals have been directed.

4. The real and substantial challenge that is presented by the appellants" learned advocate is on the basis of a relatively long line of judicial decisions in all of which similar activities have been construed by the courts has not to come within the broad umbrella of the definition of a manufacturing unit or an industrial unit. The appellants" learned advocate has essentially relied on a Division Bench decision of this Court reported in Commissioner of Income Tax Vs. Hotel Ayodya, ; in the case of Commissioner of Income Tax v. Hotel Ayodya. The court in that instance was dealing with a plea canvassed by a hotel which had installed certain machinery to manufacture and produce food articles and the contention was that the assessee was entitled to investment allowance u/s 32A in respect of the new machinery on the ground that it was a manufacturing unit. The court had occasion to consider several other decisions and in the course of an in-depth appraisal of the law on the point, the court held that the business carried on by the assessees in that case was only a hotel business and that it cannot be called an industrial undertaking. On that occasion, this Court had occasion to deal with an earlier decision of the Kerala High Court reported in Commissioner of Income Tax Vs. Casino (Pvt.) Ltd., in the case of Commissioner of Income Tax, Kerala v. Casino (Private) Ltd. The Division Bench of the Kerala High Court, while considering a similar plea under the provisions of the Income Tax Act had occasion to go into the aspect of what precisely can be construed as "manufacture" and had occasion to rely on two other decisions Ardeshir H. Bhiwandiwalla v. State of Bombay [1961] 20 FJR 113; in relation to a process involving preparation of salt by drying water by the heat of the sun and Thomas Vs. District Judge, Alleppey, which was a case relating to fermentation of toddy. The test applied by the court at that time was as to whether a commodity in the commercial sense which is different from the raw materials has resulted. The court however had occasion to go a step further than the decision of the Kerala High Court and to conclude that as far as a hotel business is concerned, though technically the edible items that resulted could be regarded as a commodity that different from the raw materials that went into it, that on an overall view of the matter that it would be unreasonable and improper to categorise it as a manufacturing unit. Effectively, the Kerala High Court took the view that a hotel

is a trading concern mainly set up for trading and not for production or manufacturing. We need to observe here that the appellants' learned advocate has drawn our attention to the fact that the Madras High Court in the case of Commissioner of Income Tax (Central) Madras Vs. Buhari Sons Pvt. Ltd., took a similar view.

5. When the issue was before this Court in the Commissioner of Income Tax Vs. Hotel Ayodya, referred to above supra, the Division Bench of this Court had occasion to rely on an earlier decision of the Karnataka High Court reported in Koshy's Private Limited Vs. Commissioner of Income Tax, Karnataka, in the case of Koshy's Private Limited v. Commissioner of Income Tax, Karnataka. The distinction which the court was required to make in that case was that since the assessee was running several units including a department store, a bakery, etc., that it was not permissible as far as one of those units were concerned, namely the restaurant, to permit it to come within the definition of manufacturing unit. In a slightly different context, the Supreme Court had occasion to consider the position in relation to cold storage units with an entirely different process in Delhi Cold Storage Pvt. Ltd. Vs. Commissioner of Income Tax, New Delhi, having regard to the fact that the processing done by a cold storage unit bringing about some change or alteration of the goods or materials, the court held that it could only answer the definition of a processing unit and not a manufacturing unit.

6. The appellants' learned advocate placed reliance on a decision of the Supreme Court in the case of Northern India Caterers (India) Ltd. Vs. Lt. Governor of Delhi, wherein, the Supreme Court had occasion to go into the nature and scope of the activity carried out by a hotel or a restaurant. The question arose as to whether supply of meals to customers in a restaurant run by a hotel could attract sales tax and the Supreme Court followed the principle originally laid down in Electa B. Merrill v. James W. Hodson LRA 1915-B 481 wherein the English Courts had occasion to analyse the situation and uphold the view that effectively the supply of food to customers under these circumstances came within the broad aspect of hospitality business and that consequently, it would not attract sales tax. Appellants' learned advocate submits that his clients basically are in the food business and that the products which they produce are meant for the consumption of customers who come to the restaurant. He states that admittedly such customers would be entitled to buy some of these items and carry them away and having regard to the fact that the quality is of a high order and has obtained a lot of popularity, that particularly at festival times, larger quantities of some of these items are required to be produced as there is a considerable amount of additional outside sale apart from what is consumed in the premises itself. He therefore submits that factually this activity is an extension of what is carried on in the restaurant and that therefore, the ratio laid down by the Supreme Court in the aforesaid decision would apply squarely to the facts of the present case.

7. The learned advocate who represents the department has strongly refuted

these contentions. He draws a basic distinction between a case of running a restaurant simpliciter and between the activity carried out by the present appellants. He has even submitted that in a given instance where essentially a business is limited to the supply of edibles and beverages within the premises of a restaurant is concerned, that the position might be slightly different. But he lays emphasis on the fact that the main reason why the tax authorities were required to revise the present assessment orders was because of the extremely large turnover in the present case. He submits that the amended definition of explanation I to entry No. 16-B has for good reason laid down a relatively high turnover limit of Rs. 10 lakhs and he submits that when one reaches this limit it is very clear that it is commercial activity carried out on a very large scale, which in his submission would bring the enterprise within the definition of a manufacturing unit or an industrial unit for purposes of entry No. 16-B. What the learned advocate submits basically is that having regard to this volume, it ceases to be a restaurant simpliciter and that consequently, the provisions of the Act are attracted. In this regard, he further submits that even as far as the facts are concerned, that in order to cater to this volume of turnover that the processes themselves would have to be on a scale that is equitable to an industry. As an example, the learned advocate quoted situations whereby even handicrafts or edible items are produced on an extremely large scale and commercially marketed and one instance that he put forward to the court was in respect of the production of biscuits, which may not be produced by a large company or industrial house which would come within the conventional definition of an industry or a manufacturing unit. He also submitted that it is really the volume and the scale on which the activity is carried out, which is the distinguishing and outstanding factor. As far as the views expressed by both the Supreme Court and the various High Courts are concerned in the decisions quoted by us, the learned advocate sought to draw a distinction in so far as he submitted that for purposes of application of various provisions of tax laws it is very necessary to fall back heavily on technicalities and that those were all decisions under the Income Tax Act and Sales Tax Act, whereas we are here considering an entirely different statute and he therefore submitted that the legislative intent as far as the present statute is concerned will have to be differently construed.

8. As indicated by us earlier, that short point that has fallen for decision in this controversy, which undoubtedly is an interesting one is the question as to whether the appellants who admittedly are producing edible items and whose annual turnover is relatively large are liable to the incidence of entry tax as far as the ingredients of some of those items are concerned. In our considered view, the exact nature of the business carried on by the appellants is of some consequence because the appellants are not running a small eating house or a restaurant but admittedly, there is a large or a bulk of the activity that relates to a virtually commercial sale of these products and if one were to look at the facts, it perhaps reaches the highest point during the festival periods, but round the year this activity does continue. Under these circumstances we do consider that

the distinction drawn by the learned Government Advocate is one of consequence in so far as the appellants' business cannot be equated on par with a mere restaurant. Also, we have taken special note of the fact that after the amendment, the definition of the term manufacturing unit or industrial unit as far as the present Act is concerned, is an omnibus one in so far as it merely goes into the aspect of scale or volume of turnover. It is very clear therefore that what the Legislature intended was that small domestic units would have to be kept outside the scope of the Act. But where the activity was of the order of Rs. 10 lakhs and above and where undoubtedly it is commercial activity done on a relatively large scale that it would have to be equated on par with a manufacturing unit or an industrial unit. We do see some Justification in this for the reason that merely because the product is an edible item would not necessarily qualify immediately for exemption. Similarly, while considering the process, the learned advocate for the appellants has advanced a very strong plea that this is only a magnification of what goes on in any domestic kitchen in a household but we are unable to accept that contention because admittedly, processing of food items is also an established industry, the glaring examples being of items such as biscuits, chocolates, etc. It is in this background therefore that we are unable to accept the submission that merely because there may be a common source of supply to the restaurant as also to the rest of the production which is commercially marketed, that the appellants will ipso facto qualify for being exempted from the provisions of entry No. 16-B. In our view, the views expressed by the various courts while considering parallel provisions under the Income Tax Act and Sales Tax Act will not hold good as far as the present enactment is concerned, for the reason that entry No. 16-B does encompass a very comprehensive and omnibus entry which is very clearly lays down that it is only the financial parameters that are to be taken into account by the authorities for the purpose of assessment. We do need to however observe that this will not change the well-settled position in law that has been pointed out by the appellants' learned advocate, as far as the activities carried on by the appellants within the four corners of their restaurant business is concerned. To that extent, a distinction will have to be drawn in so far as the assessing authority will have to separately construe that part of the production which is sold within the restaurant and that part of it which is commercially marketed.

9. In the view that we have taken, the appeal partially succeeds. The order of the reviewing authority is modified to the extent that the assessing authority shall after giving an opportunity to the appellants to produce whatever material they so desire hear them and reassess the incidence of tax as far as the concerned items go taking into account however the fact that as far as that part of the turnover which is confined to their restaurant or eating house is concerned, that it would necessarily have to be exempted. It is clarified, that the exempted part of the turnover would be limited only to that which is consumed within the premises and not that part of it which is commercially marketed.

10. The appeals partially succeed and stand disposed of. In the circumstances of

the case there shall be no order as to costs.

11. Appeals partly allowed.